STATE OF ARIZONA

Joint Legislative Budget Committee

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JOINT LEGISLATIVE BUDGET COMMITTEE
Thursday, December 16, 2004
9:30 a.m.
Senate Appropriations Room 109

MEETING NOTICE

- Call to Order

- Approval of Minutes of November 17, 2004.

- DIRECTOR'S REPORT (if necessary).

- EXECUTIVE SESSION - Consideration of JLBC Staff Director Salary pursuant to A.R.S. § 38-431.03.

1. ARIZONA DEPARTMENT OF ADMINISTRATION
   A. Consider Approval of Mileage Reimbursement for State Travel by Motor Vehicle and Aircraft.
   B. Consider Approval of Maximum Lodging Reimbursement Rates.

2. STATE COMPENSATION FUND - Consider Approval of Calendar Year 2005 and 2006 Budgets.

3. DEPARTMENT OF PUBLIC SAFETY - Quarterly Review of the Arizona Public Safety Communications Advisory Commission.

4. JOINT LEGISLATIVE BUDGET COMMITTEE - Consider Approval of Year 2005-2006 Strategic Program Area Review Topic Candidates.

5. ARIZONA DEPARTMENT OF TRANSPORTATION - Review of an Intergovernmental Agreement Between Arizona Department of Transportation and Maricopa County (Phoenix International Raceway).

6. DEPARTMENT OF ECONOMIC SECURITY - Review of Expenditure Plan for Workforce Investment Act Monies.

7. GOVERNOR'S OFFICE OF STRATEGIC PLANNING AND BUDGETING - Report on Federal Revenue Maximization Initiative.

8. ATTORNEY GENERAL - DEPARTMENT OF LAW - Report on New Staffing of Child Protective Services Attorneys.

9. ARIZONA STATE RETIREMENT SYSTEM - Report on Contribution Rates.

The Chairman reserves the right to set the order of the agenda.
12/9/04

People with disabilities may request accommodations such as interpreters, alternative formats, or assistance with physical accessibility. Requests for accommodations must be made with 72 hours prior notice. If you require accommodations, please contact the JLBC Office at (602) 542-5491.

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MINUTES OF THE MEETING

JOINT LEGISLATIVE BUDGET COMMITTEE

November 17, 2004

The Chairman called the meeting to order at 9:53 a.m., Wednesday, November 17, 2004, in Senate Appropriations Room 109. The following were present:

Members:	Senator Burns, Chairman	Representative Pearce, Vice-Chairman
	Senator Anderson	Representative Biggs
	Senator Cannell	Representative Burton Cahill
	Senator Harper	Representative Lopez
	Senator Martin	
	Senator Rios	
Absent:	Senator Arzberger	Representative Farnsworth
	Senator Bee	Representative Gray
		Representative Huffman
		Representative Huppenthal

APPROVAL OF MINUTES

Senator Burns moved *that the Committee approve the minutes of October 14, 2004.* The motion carried.

EXECUTIVE SESSION

Senator Anderson moved *that the Committee go into Executive Session.* The motion carried.

At 9:55 a.m., the Joint Legislative Budget Committee went into Executive Session.

Representative Pearce moved *that the Committee reconvene into open session.* The motion carried.

At 10:35 a.m. the Committee reconvened into open session.

Representative Biggs moved *that the Committee approve the state going to trial in the case of Irasema Gomez v. Officer Frank Torres, the Arizona Department of Public Safety, and the Arizona Department of Transportation*. By a show of hands the motion failed.

Senator Anderson moved *that the Committee approve the recommended settlement proposal by the Attorney General's Office in the case of Irasema Gomez v. Officer Frank Torres, the Arizona Department of Public Safety, and the Arizona Department of Transportation*. The motion carried.

Due to a lack of a quorum, Chairman Burns adjourned the meeting at 10:35 a.m.

Respectfully submitted:

Cheryl Kestner, Secretary

Richard Stavneak, Director

Senator Bob Burns, Chairman

NOTE: A full tape recording of this meeting is available at the JLBC Staff Office, 1716 West Adams.

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DATE: December 9, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Shelli Carol, Fiscal Analyst

SUBJECT: Arizona Department of Administration – Consider Approval of Mileage Reimbursement for State Travel by Motor Vehicle and Aircraft

Request

A.R.S. § 38-623.D requires the Arizona Department of Administration (ADOA) to set the rates of reimbursement for state travel by motor vehicle and by airplane, taking into consideration the amounts established by the United States Internal Revenue Service (IRS). The rates compensate state employees who use their own vehicles to travel on official state business. The statute also mandates Committee approval of any rate change.

ADOA requests Committee approval for an increase in the mileage reimbursement rates, from 34.5 cents per mile to 37.5 cents per mile for motor vehicles, and from 42.0 cents per mile to 99.5 cents per mile for aircraft. The proposed rates are consistent with federal reimbursement levels. If the Committee approves the suggested rates, ADOA asks that the adjustments become effective immediately.

Recommendation

The Committee has at least the following options:

1) Approve the rates as submitted. The various agencies of the state would have to absorb additional travel costs. ADOA estimates the annual fiscal impact of the changes on state agencies would be $303,000 among all funds. Meanwhile, the state universities could not all isolate mileage expenditures, but they calculated a combined annual increase greater than $149,000 from all funds.

   Committee approval would not constitute an endorsement of additional appropriations to cover higher travel costs. Agencies may request funding increases through the regular budget process.

(Continued)

2) Not approve the new rates. State employees would continue to absorb additional travel costs.

3) Request that ADOA report to the Committee by April 15, 2005 on the establishment of different motor vehicle rates, depending on the availability of state motor pool vehicles. For example, the federal government reimburses 37.5 cents per mile when a government vehicle is not available, but only 27 cents per mile when government-owned vehicles are available and an employee chooses not to use one. The department has expressed its willingness to implement this policy for all Executive branch fleets and reports that ADOA generally available short-term-use vehicles are currently employed at 63.5% of capacity.

   At a minimum, the report would contain annual usage impact on the various fleets; annual personnel and cost impact on the various fleets; all anticipated fleet rate increases to agencies; annual savings to state agencies by fund type; any safety or liability concerns and a plan for mitigating them; and an explanation of how the requested estimates were derived. This option could also be combined with either Options 1 or 2.

Analysis

Annually, the federal government hires a specialized transportation-consulting firm to study nationwide travel market conditions. Factors considered include the average costs of depreciation, maintenance, repairs, fuel, and insurance. On January 1, 2004, the U.S. General Services Administration (GSA) published the current travel reimbursement rates of 37.5 cents per mile for motor vehicles and 99.5 cents per mile for aircraft. These rates serve federal government internal reimbursement purposes and IRS tax purposes.

The current IRS rates likely represent a conservative estimate of travel expenses. In its newest Employer's Tax Guide, the IRS allows private employers to begin reimbursing their employees at 40.5 cents per mile on January 1, 2005. To date, however, the GSA has not increased reimbursement levels for federal government employees.

The current GSA rates are based on an average gasoline price from late 2003, $1.53 per gallon. As of December 3, Arizona's average fuel price was $2.02 per gallon, while the national average was $1.94 per gallon. Additionally, ADOA has assessed that auto insurance rates in Arizona are above the national average. The most recent statistics published by the National Association of Insurance Commissioners reflect data from calendar year 2002 and rank Arizona 11th in the nation, up from 14th in calendar year 2001. Arizona's average annual car insurance premiums were more than $110 above the national average in 2002.

At its February 2001 meeting, the Committee approved a motor vehicle mileage rate increase from 32.5 cents per mile to the current 34.5 cents per mile. ADOA requested another motor vehicle rate increase at the Committee's November 2002 meeting, hoping to raise the rate from 34.5 cents to 36.5 cents per mile. The Committee did not approve the change, due to concerns over the availability of funding. Meanwhile, the Committee approved the current aircraft mileage rate of 42.0 cents per mile in March 1995.

The current request of a motor vehicle rate change from 34.5 cents per mile to 37.5 cents per mile represents an 8.7% increase. ADOA asks that the increased reimbursement rate go into effect immediately upon Committee approval. Across state agencies, ADOA approximates that the new rates would have an annualized impact of $66,000 on the General Fund and $237,000 on all other appropriated and non-appropriated funds.

(Continued)

Although they are not mandated to do so, the state's public universities also use ADOA mileage reimbursement rates. Arizona State University reports that the motor vehicle rate change would increase yearly travel expenditures from all state funds by $14,000 and from all non-appropriated funds by $33,000. Meanwhile, Northern Arizona University estimates an annual impact of $33,000 among state funds and $69,000 among non-appropriated funds. The University of Arizona could not isolate mileage costs from other travel expenses. The ADOA and university calculations assume that miles traveled by employees would remain at FY 2004 levels.

No Arizona state or public university employees travel on official business using private aircraft. The ADOA Risk Management Division ceased providing insurance coverage for this transportation mode several years ago. Therefore, the air travel rate change would have no foreseeable fiscal impact at the state level. However, it is the policy of many of the state's political subdivisions to adopt the rates set by the Committee. Employees of those subdivisions using private aircraft on official business currently absorb a large share of their own travel costs.

RS:SC:ss

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DATE: December 9, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Shelli Carol, Fiscal Analyst

SUBJECT: Arizona Department of Administration – Consider Approval of Maximum Lodging Reimbursement Rates

Request

A.R.S. § 38-624.C requires the Arizona Department of Administration (ADOA) to establish maximum amounts for lodging reimbursement, taking into consideration the amounts established by the federal government. The rates compensate state employees traveling on official state business. The statute requires Committee approval of any rate change.

ADOA proposes increasing the standard lodging rate, used for markets not explicitly listed, from $55 to $60 per day. The department also seeks overall decreases to in-state lodging rates and overall increases to out-of-state rates. If the Committee approves the suggested rates, ADOA asks that the adjustments become effective immediately.

Recommendation

The Committee has at least the following options:

1) Approve the rates as submitted. The requested rates are consistent with or below federal reimbursement levels. The various agencies of the state would have to absorb additional travel costs. ADOA estimates the annual fiscal impact of the changes on state agencies would be $664,000 among all funds. Meanwhile, the universities anticipate a combined annual expenditure increase of approximately $1.4 million from all funds.

   Committee approval would not constitute an endorsement of additional appropriations to cover any higher travel costs. Agencies may request funding increases through the regular budget process.

2) Not approve the new rates. State employees would continue to absorb additional travel costs.

(Continued)

Analysis

At its November 2000 meeting, the Committee approved the current lodging reimbursement schedule. ADOA made another lodging rate increase request at the Committee's November 2002 meeting. The Committee did not approve those changes due to concerns over the availability of funding.

Annually, the federal government conducts a national cost survey of travel market conditions and uses the resulting data to update its internal lodging reimbursement rates. The U.S. General Services Administration published the most recent reimbursement schedule on October 1, 2004. The federal schedule specifies rates for many cities, with seasonal distinctions in some cases. The schedule also includes a standard rate of $60 for all other locations.

ADOA seeks to align Arizona's out-of-state lodging rates with federal guidelines. Overall, these changes would represent an approximate 10% increase to lodging reimbursements. Across state agencies, ADOA approximates that the new rates would have an annualized impact of $124,000 on the General Fund and $540,000 on all other appropriated and non-appropriated funds.

Although they are not mandated to do so, the state's public universities also use ADOA lodging reimbursement rates. The three universities report that the lodging rate change would increase yearly travel expenditures between $168,000 and $198,000 from all state appropriated funds, as well as by approximately $1.2 million from all non-appropriated funds.

ADOA has identified the top 20 out-of-state markets where Arizona state employees travel most often on official business. Current rates in these locations range from $55 to $159. ADOA proposes increases of up to $50, with an average of $18, in 18 markets. Travelers to Las Vegas, Nevada would obtain the largest increases. At the same time, ADOA recommends decreases of up to $(33), with an average of $(21), at 2 locations. Travelers to San Francisco, California would experience the largest decreases. Overall, ADOA requests new rates ranging from $60 to $153 in these 20 markets.

Among all other out-of-state markets, present rates range from $55 to $215. ADOA suggests increases of up to $126, with an average of $21, in 666 geographic/seasonal markets. Travelers to Aspen, Colorado would receive the largest increases. The department also recommends decreases of up to $(73), with an average of $(16), in 158 geographic/seasonal markets. Travelers to Boston, Massachusetts would be among those seeing the largest decreases. Overall, the proposed out-of-state rates range from $60 to $249.

Within the Arizona market, ADOA believes it has a better understanding of travel cost conditions than that reflected by the federal travel survey. Therefore, the department recommends certain lower rates for in-state travel.

ADOA currently defines 8 markets for travel in Arizona. Existing in-state lodging rates range from $55 to $107. The department suggests increases of up to $28, with an average of $12, in 4 of those markets. Travelers coming to Maricopa County would receive the largest increases. Meanwhile, ADOA seeks decreases of up to $(38), with an average of $(15), in 4 markets. Travelers to Apache County would see the largest decreases. Overall, the proposed in-state rates range from $60 to $107.

ADOA proposes raising the standard reimbursement rate for all non-specified in-state and out-of-state markets from $55 to $60, representing a 9.1% increase. The department has also adjusted the seasonal timeframes of several locations to match federal changes and to better reflect current travel market conditions. ADOA asks that the increased lodging reimbursement rates go into effect immediately upon Committee approval.

(Continued)

In certain circumstances, maximum lodging rates do not apply. Many hotels set a government rate using the most recent federal schedule and charge that daily rate to all government employees, even state employees. In situations where the federal rate is higher than the state rate, employees often request waivers from the ADOA General Accounting Office (GAO) to reimburse their additional costs. GAO encourages state employees to receive approval for such requests in advance. Since July 1, 2004, GAO granted waivers for 167 travel claims out of 11,200 processed, representing 1.5% of the total. Additionally, when state employees receive prior authorization to attend a conference on official state business, they may obtain reimbursement for their stay at the conference hotel regardless of the daily charge.

RS:SC:ss

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DATE: December 9, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Eric Jorgensen, Fiscal Analyst

SUBJECT: State Compensation Fund – Consider Approval of Calendar Year 2005 and 2006 Budgets

Request

Pursuant to A.R.S. § 23-981E, the State Compensation Fund (SCF) budgets for Calendar Year (CY) 2005 and CY 2006 are submitted for approval by the Joint Legislative Budget Committee. Unlike state agencies, the State Compensation Fund is budgeted on a calendar year basis rather than a fiscal year basis.

As detailed in *Attachment 1,* the SCF requests a budget of $89,540,000 for CY 2005. This includes an operating budget of $51,500,000 and Special Line Items (SLI) that total $38,040,000. The SLIs are largely driven by market forces.

The SCF requests a budget of $93,565,000 for CY 2006. This includes an operating budget of $53,200,000 and SLIs that total $40,365,000. The request represents a net increase of 4.5% above the CY 2005 recommended budget.

The requested amounts do not include any dividend or claims paid by the SCF. No request for Capital Outlay has been made.

Recommendation

The committee has at least 3 options in reviewing the requested budget:

1. Approve the budget as requested.

(Continued)

2. Approve the budget as requested, but adjust the salary increase to be in line with statewide employee salary increases approved by the Legislature for FY 2005.
3. Take no action. SCF does not believe that the Committee's action limits their budget. The Committee never approved a FY 2004 budget. In FY 2001 to FY 2003, SCF's expenditures exceeded the approved level of spending.

Analysis

The SCF has requested an operating budget of $89,540,000 in CY 2005 and $93,565,000 in CY 2006. This represents an increase of $14,455,000 or 19.3%, above CY 2004 expenditures for CY 2005 and $18,480,000 in CY 2006 (see *Attachment 1*). Of the requested amount, $11,255,000 in CY 2005 and $13,580,000 in CY 2006 is for Special Line Item increases in claim adjustment services, rating bureau fees, premium taxes, administrative fees and property taxes. These SLIs are driven by market forces and claim volume, giving SCF little control over these costs.

The request includes increased funding of $3,200,000 in CY 2005 and $4,900,000 in CY 2006 for the operating budget. This amount includes Personal Services and Employee Related Expenditures increases equal to an average salary increase of $1,300 per employee. Most state employees received a $1,000 increase for FY 2005. Traditionally, the Committee has aligned SCF salary increases with state employee pay.

The request also includes a 7% increase in CY 2005 and 13% in CY 2006 for other operating expenses, including travel, equipment and professional services. Claim volume is expected to increase by 6% in CY 2005 and by 11% in CY 2006 over CY 2004. Also, professional service expenses have increased due to a change to external management of fixed income investments. SCF reports a market share of about 50% of the statewide premium dollar and approximately 60-65% of all Arizona employers.

Table 1 shows the historical changes in premium and investment income, and the number of policyholders and claims.

Table 1

STATE COMPENSATION FUND
Growth in Premium Income, Investment Income, Policyholders and Claims Processed

	Actual 2003	Estimated 2004	Estimated 2005	Estimated 2006
Premium Income (in Millions)	$341.0	$353.0	$360.0	$370.0
Dollar Increase	65	12	7	10
Percentage Increase	23.5%	3.5%	2.0%	2.8%
Investment Income (in Millions)	$160.1	$182.0	$129.0	$130.0
Dollar Increase	32	22	(53)	1
Percentage Increase	24.9%	13.7%	-29.1%	0.8%
Policyholders	53,953	55,372	56,000	57,000
Dollar Increase	1,756	1,419	628	1,000
Percentage Increase	3.4%	2.6%	1.1%	1.8%
Claims Processed	49,268	53,270	56,500	59,000
Dollar Increase	3,934	4,002	3,231	2,500
Percentage Increase	8.7%	8.1%	6.1%	4.4%

(Continued)

There are some matters of concern regarding the SCF budget process. SCF expenditures in CY 2001, CY 2002 and CY 2003 exceeded amounts approved by the Committee. In CY 2003, SCF exceeded the approved operating expenditures by $3.9 million, or 9% and the Special Line Item expenditures by $5.6 million, or 24%. Some of the components of the SCF budget, such as number of policy holders, claims and management fees, are workload and market driven, and as a result may be difficult to predict. These are the Special Line Items listed in *Attachment 1*. However, the administrative component of the SCF budget has also been increased above the amount approved by the Committee, primarily for salary increases.

Further, at the December 20, 2002 JLBC meeting, the Committee only approved the CY 2003 budget. The SCF did not submit a CY 2004 budget the following year and no budget for CY 2004 was ever approved. Nevertheless, in CY 2004, SCF spent $75.1 million.

SCF's willingness to reject the Committee's decision has probably been strengthened by the Maricopa Superior Court ruling of April 13, 2004 that "the monies and assets held by the State Compensation Fund are not public funds." This ruling stemmed from a dispute over whether the Legislature could transfer monies from the SCF to the General Fund. The ruling found that "the proposed transfer from the State Compensation Fund to the State General Fund . . . would violate the Arizona Constitution."

Finally, we also note that SCF has announced its intention to participate in the Knowledge Economy Capital Fund. This group is intended to address the lack of venture capital in the state. SCF will contribute up to $25 million of the planned $100 million to provide venture capital to emerging companies. This will be an investment asset for SCF, and there is a high level of associated risk.

The Chairman submitted additional questions to SCF after the November meeting. SCF's response to these questions is found in Attachment 2.

RS/EJ:jb
Attachments (2)

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DATE: November 5, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Martin Lorenzo III, Assistant Fiscal Analyst

SUBJECT: Department of Public Safety – Quarterly Review of the Arizona Public Safety Communication Advisory Commission

Request

Pursuant to Laws 2004, Chapter 281 the Department of Public Safety (DPS) has submitted for review their FY 2005 1st quarter expenditures and design progress for the statewide interoperability design project.

Recommendation

The JLBC staff recommends that the Committee give a favorable review of the request. First quarter expenditures totaled $249 out of $5,000,000 in available funding. An Executive Director and 1 staff position have been hired for the Public Safety Communication Advisory Commission (PSCC.)

Analysis

Background
Laws 2004, Chapter 275 appropriated $5 million to DPS for design costs of a statewide radio interoperability communication system. Radio interoperability allows public safety personnel from one agency to communicate, via mobile radio, with personnel from other agencies. An interoperable system enhances the ability of various public safety agencies to coordinate their actions in the event of a large-scale emergency as well as daily emergencies. Construction costs of a statewide radio interoperability communication system are estimated to be as high as $300 million.

First Quarter Expenditures
In the first quarter of FY 2005, DPS and PSCC report expenditures totaling $249. This amount consisted of advertising costs for the Executive Director and Administrative Services Officer positions. The following table shows the expenditure plan submitted to the Committee at its June 2004 meeting.

(Continued)

Table 1

FY 2005 Statewide Interoperability Design Expenditure Plan

	$5 Million Appropriation [1/]
FTE Positions	9.0
Personal Services	$ 382,800
Employee Related Expenditures	104,200
Professional and Outside Services	4,040,500
Travel – In	20,700
Travel – Out	15,900
Other Operating Expenditures	338,700
Equipment	97,200
Total Operating Expenditures	**$ 5,000,000**

1/ The additional $3 million appropriated by Chapter 275 is non-lapsing and is included in the Professional and Outside Services line.

Current Updates

On October 1, 2004, DPS named Curt Knight as the Executive Director of the PSCC, concluding the selection process that began in August. An Administrative Services Officer was hired shortly thereafter. Currently, PSCC is working on recruiting an Executive Assistant as well as advertising for qualifying Telecommunications Engineers. In total the PSCC would hire 9 FTE Positions. Office space for the support office has been leased and telephone services and hardware have been ordered.

In accordance with Laws 2004, Chapter 275, the Executive Director has contacted the Government Information and Technology Agency confirming the establishment of the Commission as well as extending an invitation to the first Commission meeting that was held on October 26, 2004.

These updates will be reflected in review of the second quarter expenditures.

RS/ML:jb

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DATE: December 8, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Stefan Shepherd, Assistant Director

SUBJECT: Joint Legislative Budget Committee – Consider Approval of Year 2005-2006 Strategic Program Area Review Topics Candidates

Request

The Joint Legislative Budget Committee (JLBC) Staff requests that the Committee approve the list of program areas to be reviewed in the Year 2005-2006 Strategic Program Area Review (SPAR) process. The intent of the SPAR process is to review issues that often involve multiple agencies and evaluate the efficiency, effectiveness, and necessity of the programs administered.

Recommendation

The JLBC Staff recommends the following 4 program areas for the Year 2005-2006 SPAR cycle:

- Workforce Development
- Homeland Security
- University Financial Aid
- Ports of Entry

Analysis

A.R.S. § 41-1275 requires that JLBC Staff, "in consultation with" OSPB, recommend to the Committee by January 1 of each odd-numbered year a list of program areas for SPAR. The SPAR process is designed to look at issues that involve multiple agencies and consists of three parts: 1) self-assessment by participating agencies, 2) review of the self-assessment by JLBC Staff and OSPB and recommendations to retain, eliminate, or modify the programs, and 3) legislative review.

(Continued)

The Committee "shall determine those program areas that are subject to [SPAR] from the list of program areas submitted" by JLBC Staff. Statute says that agencies may submit suggestions for the SPAR process. JLBC Staff received suggestions from two agencies: Office of Tourism (assorted programs) and Department of Economic Security (job placement privatization).

JLBC Staff recommends the following 4 program areas for the Year 2005-2006 SPAR cycle:

- <u>Workforce Development</u>: The Department of Economic Security administers the federal Workforce Investment Act grant, administers job training programs for welfare clients, and runs vocational rehabilitation programs. The Department of Commerce administers the Arizona Job Training Fund and runs other workforce development programs. This SPAR would review workforce development programs in these agencies as well as in the Department of Education, community colleges, Universities, and the Governor's Office.
- <u>Homeland Security</u>: The Arizona Office of Homeland Security administers homeland security grant monies received from the federal Department of Homeland Security for law enforcement and security threats. The Arizona Department of Health Services administers homeland security grant monies received from the federal Department of Health and Human Services for bioterrorism and public health threats. In FY 2003, these two grant programs provided monies to over a dozen state agencies in additional to several local governments. To date, the majority of FY 2004 monies have not been awarded. This SPAR would review the allocation and expenditure of grant monies in these agencies.
- <u>University Financial Aid</u>: There are a variety of fund sources that are available for financial aid for students attending the state universities. This SPAR would attempt to provide a comprehensive review of available financial aid relative to financial aid need within the university system.
- <u>Ports of Entry</u>: The Arizona Department of Transportation's Motor Vehicle Division administers commercial vehicle compliance with the state's weight, licensing, permit, and tax laws at the ports. The Arizona Department of Agriculture uses the ports to screen trucks and their cargo to intercept agricultural pests, weeds, and livestock diseases. The Department of Public Safety maintains a limited field presence at some ports to perform safety inspections of commercial vehicles along with other patrol and field duties. This SPAR would review port of entry use, coordination and cooperation in these agencies. Arizona Ports of Entry were previously the subject of a SPAR in FY 2000.

If these 4 program areas are selected as SPAR candidates, JLBC Staff and OSPB will send out instructions to relevant agencies. Agencies are required to submit their self-assessments to OSPB and JLBC Staff by June 1, 2005. JLBC Staff and OSPB "shall jointly produce a report of their findings and recommendations for whether to retain, eliminate or modify funding and related statutory references for the programs" and submit that report to the President of the Senate, the Speaker of the House of Representatives, and the Governor by January 1, 2006. The President and Speaker are required to assign the SPARs to the Appropriations Committees and may also assign the SPARs to relevant standing committees; at least one public hearing is required on each SPAR.

RS:SSh:ss

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Joint Legislative Budget Committee

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DATE: December 8, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Lorenzo Martinez, Assistant Director

SUBJECT: Arizona Department of Transportation - Review of an Intergovernmental Agreement Between Arizona Department of Transportation and Maricopa County (Phoenix International Raceway)

Request

The Arizona Department of Transportation (ADOT) and Maricopa County request Committee review of the intergovernmental agreement related to the design, reconstruction and improvement costs of highway improvements to enhance access to a sports entertainment facility (Phoenix International Raceway). Committee review is required pursuant to the authorizing legislation (Laws 2004, Chapters 182 and 282).

Recommendation

The JLBC Staff recommends that the Committee give a favorable review of the request. The agreement contains the items required by the authorizing legislation, as well as additional statutory references and technical language changes suggested by Legislative Council.

The agreement and authorizing legislation stipulate the transfer of up to $416,667 annually from state sales collections between FY 2008 and FY 2019 for the state's obligation in financing the highway improvements. Transfers from the sales tax total $5,000,000 over the 12-year period. Maricopa County is responsible for any project costs above the state contribution. If major ownership interest in the facility changes before June 30, 2014, the county is responsible for reimbursing the state for sales tax transfers to date.

Analysis

Laws 2004, Chapters 182 and 282 authorized the use of state sales tax revenues to help pay for highway improvements to a sports facility (as defined in A.R.S. § 42-5032), if the facility is selected as the site of an additional major national sporting event by December 31, 2004. Phoenix International Raceway (PIR) has been awarded a second NASCAR race beginning in Spring 2005. As a result of anticipated increased

(Continued)

sales tax collections from the additional event, the legislation allows the transfer of up to $416,667 annually from state sales tax collections over a 12-year period beginning in FY 2008 to help pay for highway improvements to enhance access to PIR. Transfers over the 12-year period would total $5,000,000. Any costs for the project that are above the state contribution will be paid by Maricopa County. Preliminary cost estimates for the project are $5,100,000.

A similar arrangement was authorized in 1997 for construction of a bridge to improve access to PIR. Funding for the bridge project included $3,719,150 from Maricopa County, $1,284,000 from the City of Avondale, $4,627,000 from federal funds, $350,000 from the Corporation Commission Economic Strength Program, and $5,000,000 million from state sales tax collections. State sales tax monies of $416,667 were to be transferred annually between FY 1999 and FY 2010. The project was completed in 1999. State sales tax transfers are used to reimburse the county for advancing funding for the project.

While the county is authorized to issue bonds for the new highway improvement project if the county board of supervisors also authorizes the bond issuance by December 31, 2004, Maricopa County does not plan on issuing bonds to finance the project. The county will provide advance funding for the project and the annual transfers of state sales tax will reimburse the county. The Maricopa County Board of Supervisors is scheduled to review the 2 related agreements between ADOT and the county, and PIR and the county on December 15, 2004. The Committee is only required to review the agreement between ADOT and the county. The agreement between PIR and the county is attached as an informational item.

Chapters 182 and 282 required the agreement to include:

- Commitment of state and county to provide monies to finance the project.
- Outline of the responsibilities of each party regarding planning, design, construction, owning and maintenance of highway.
- Provide that payment for costs be made from other available contributions before use of state sales tax amounts.
- Provide that the county reimburse the state General Fund for sales tax transfers to date if major ownership interest in the facility is conveyed before June 30, 2014.
- Allow county to enter into agreement with sports facility to have owner of facility reimburse the county for expenses if the ownership of the facility changes before June 30, 2014.

The submitted agreement addresses the required items.

RS/LM:jb

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HOUSE OF REPRESENTATIVES

DATE: December 9, 2004

TO: Representative Russell Pearce, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: John Malloy, Fiscal Analyst

SUBJECT: Department of Economic Security- Review of Expenditure Plan for Discretionary Workforce Investment Act Monies

Request

Pursuant to a footnote in the General Appropriation Act, the Department of Economic Security (DES) is submitting an expenditure plan for $2.2 million in discretionary federal Workforce Investment Act (WIA) monies received by the state for FY 2005. Unlike most federal funds, the WIA monies are subject to legislative appropriation due to federal requirements. These monies cannot be spent until an expenditure plan has been reviewed by the Joint Legislative Budget Committee.

The Committee favorably reviewed $2.5 million in discretionary WIA expenditures in June 2004. Those monies represented core functions typically funded with WIA dollars. The December 2004 expenditure plan reflects items that are more discretionary.

Of the $2.2 million in proposed funding, $639,300 is one-time funding.

Recommendation

The Committee has at least the following three options:

1. A favorable review of DES' plan for $2.2 million in discretionary WIA expenditures.
2. Deferring a decision on the expenditure plan until DES provides more information on the new programs proposed by the Governor's Council.
3. An unfavorable review.

Since DES' request has raised numerous questions, JLBC Staff has asked DES for additional information. At the time of publication, Staff has not received a response from the agency. Where appropriate, Staff's specific questions have been included in the text of the program's description.

In September 2003, DES submitted an expenditure plan for WIA monies that included $1.8 million in discretionary program expansions. At that time, the Committee chose to defer discussion on these program expansions in order to determine if those monies could be used to solve FY 2004 shortfalls within DES' budget. The option to utilize WIA dollars became immaterial when DES received a supplemental appropriation that addressed all of the agency's FY 2004 shortfalls. As a result, the Committee favorably reviewed the $1.8 million expenditure plan in June 2004.

Analysis

The DES Workforce Development Administration (WDA) is the state's grant recipient for federal WIA funds from the U.S. Department of Labor. The WIA legislation established block grants to states for workforce development. Funds are delivered to the local level to those in need of services, including job seekers, dislocated workers, youth, veterans, disabled individuals and employers. Services are provided through partnerships between various public and private sector employment and training agencies.

The Governor's Council has recommended the establishment of $1.0 million in new programs in FY 2005. The new programs include Training for Local Workforce Investment Areas, Local Labor Market Information, Early Childhood Scholarships and High Technology Education. There is also funding for a Master Teacher Program, which was funded with an unknown allotment of "Youth Programs" monies in FY 2004. There is a table at the end of this memo that delineates discretionary funding for both FY 2004 and FY 2005. The table includes programs to be reviewed by the Committee as well as funding that was approved at the June 2004 JLBC Meeting.

New Programs

Training For Local Workforce Investment Areas
Monies will provide $170,000 in technical assistance to local workforce investment areas (LWIAs) that fail to meet local performance measures, in addition to local areas in their continued delivery of services through the One-Stop system.

JLBC Staff Question:
Training for LWIA Board and staff members is listed as a required activity. Was this issue funded in FY 2004?

Local Labor Market Information
Funding will allow the Governor's Council on Workforce Policy and the Arizona Department of Commerce to coordinate and implement an outreach program emphasizing Labor Market Information (LMI) access and targeted training throughout the state to enable job seekers, educators, economic developers, and business leaders to make better decisions. The requested level of funding for this program is $180,000.

JLBC Staff Question:
What agency would be the recipient of Labor Market Information monies? We had given Commerce $250,000 in FY 2003 for Business Research and Statistics. Is this program similar to that initiative? Was this issue funded in FY 2004? Are there any FTEs associated with this funding?

Early Childhood Scholarships
These funds ($433,000) will continue the efforts of the School Readiness Board to impact school readiness by providing an opportunity for early childhood educators to obtain quality professional development and leadership development. The scholarship program will continue to focus on the metropolitan areas and the under-served rural populations.

JLBC Staff Question:
How many individuals are expected to receive scholarships for early education training? Is all of the $433,000 being used for scholarships, or is there an administrative component? The rationale indicates that the scholarship will continue the efforts of the School Readiness Board. Are WIA funds being used to supplant funding for the School Readiness Board for this program? If so, what funding source is WIA replacing? Please provide data on the number of individuals receiving scholarships and any other performance measures for this initiative for FY 2004

High Technology Education
The focus of these funds ($250,000) will be on developing cross-training programs with Aerospace/Defense and Semiconductor industries. Training will be designed to address the industry specific differences to ensure a smooth transition of talent to fill workforce gaps from one industry to another.

JLBC Staff Question:
Please provide more detail on the programs to be funded with the High Tech Education Funding. What companies would receive funding? How many individuals are projected to be served?

Existing Programs

The above programs will be funded, in part, by the elimination or scaling back of $1.3 million in programs funded in FY 2004. Programs recommended to be eliminated or scaled back include monies to assist Nursing Programs at the state's Community Colleges as well as Youth and Women's Programs.

In addition to the establishment of new programs, the Governor's Council also recommended to continue to support (to varying degrees) programs funded with WIA monies in FY 2004. These include programs targeting youth, women as well as master teachers.

Youth Programs
The requested funding ($301,000) will focus on youth workforce development programs targeted to youth (ages 14-21) who have dropped out of school as youth that have dropped out of school are at a higher risk of not being prepared for future employment, to retain employment, and are more likely to earn lower wages than someone who has attained a high school diploma or G.E.D.

JLBC Staff Question:
There is $301,000 being requested for Youth Programs. A portion of that funding is for youth that have dropped out of school. How much of the $301,000 is for this specific program? How many youth are expected to be served? What type of programs will be funded? Are there any FTEs associated with this funding?

Women's Programs
Funding totaling $450,000 will focus on employing women from vulnerable and hard to serve areas including domestic violence, substance abuse, disability or divorce and involvement with the criminal justice system.

JLBC Staff Question:
The FY 2004 funding level for Women's Programs included $65,000 for a staff person to fund the grant process. Is this position being funded in FY 2005? Would the $450,000 include funding for this position? Funding has decreased $50,000 for this initiative in FY 2005. What programs are being reduced from FY 2004 as a result of the decrease in requested funding for this program?

Master Teacher Program
The requested funding of $450,000 will provide high-poverty districts with the opportunity to train and retain high quality teachers with the goal of improving teacher effectiveness and student achievement. Funds will also be utilized for professional development of new and mid-career teachers seeking additional education or national board certification, opportunities for districts to use experienced highly performing teachers as mentors and to further develop highly performing teachers as both a retention tool and as a means to improve the skill of other teachers for the purpose of improving student achievement.

JLBC Staff Question:
How many Master Teachers will receive funding with the $450,000? How much WIA funding did this program receive in FY 2004? Are there any FTEs associated with this funding?

Additional JLBC Staff Questions:
Is there a program to train child care workers in FY 2005?
Is there a Nursing Initiative Program for FY 2005?

Governor's Council Recommendation of 15% Set-Aside

Programs to be Reviewed	**Agency**	**FY 2004**	**FY 2005**	**Net Change**
Training for LWIAs	LWIA	--	$170,000	$ 170,000
Local Labor Market Information	COM	--	180,000	180,000
Early Childhood Scholarships	ADE	--	433,000	433,000
High Tech Education		--	250,000	250,000
Master Teacher	ADE		450,000	450,000
Youth Programs	LWIA	1,000,000[1]	301,000	(699,000)
Women's Programs	GOV	500,000	450,000	(50,000)
Nursing Programs	CC	510,400	--	(510,400)
Subtotal: Plan to be Reviewed		***$2,010,400***	***$2,234,000***	***$223,600***
Programs Reviewed by Committee				
Eligible Training Provider List	ADE	$214,300	$127,000	$ (87,300)
Incentive Funds for LWIAs	LWIA	500,000	500,000	--
Technical Assistance	LWIA	125,000	250,000	125,000
System Building	LWIA	152,000	300,000	148,000
High Concentration of Youth Activities	LWIA	200,000	200,000	--
Virtual One Stop	DES	325,000	325,000	--
Evaluation	GOV	--	125,000	125,000
Apprenticeship	ADOC	130,000	70,000	(60,000)
ADOC/State Council	ADOC	600,000	600,000	--
Subtotal: Plan Already Reviewed		***$2,246,300***	***$2,497,000***	***$250,700***
TOTAL 15% SET-ASIDE		**$4,256,700[2]**	**$4,731,000[3]**	**$474,300**

Legend

ADE	*Department of Education*	*LWIA*	*Local Workforce Investment Areas*
GOV	*Governor's Office*	*ADOC*	*Department of Commerce*
DES	*Department of Economic Security*	*CC*	*Community Colleges*

1/ Includes funding for Master Teacher Program
2/ Of this total, $640,000 was not expended in FY 2004
3/ Includes $640,000 in prior year funding not expended in FY 2004

RS/JM:ck

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HOUSE OF REPRESENTATIVES

DATE: December 9, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Stefan Shepherd, Assistant Director

SUBJECT: Governor's Office of Strategic Planning and Budgeting - Report on Federal Revenue Maximization Initiative

Request

Pursuant to a General Appropriation Act footnote, the Governor's Office of Strategic Planning and Budgeting (OSPB) has submitted its quarterly report on the status of a Federal Revenue Maximization Initiative.

Recommendation

This item is for information only and no Committee action is required. JLBC Staff notes that OSPB's report indicates that none of the savings for completed projects are allocated to the $25 million of savings incorporated into the overall budget.

Analysis

Laws 2004, Chapter 275, Section 80 states the following:

> "The Office of Strategic Planning and Budgeting shall report to the Joint Legislative Budget Committee by July 1, 2004 and the beginning of each subsequent calendar quarter in the fiscal year on the status of the Federal Revenue Maximization Initiative. The report, at a minimum, shall include an update on contracts awarded as a result of the "RevMax" request for proposals, a summary of projects and the potential savings from each project. Any reported savings shall distinguish between potential reductions in current funding levels and foregone future spending increases."

This provision was associated with an estimated $25 million of savings incorporated into the overall FY 2005 budget. These savings were not allocated to specific agency budgets; rather they were assumed as part of the overall "balance sheet" and were intended to reduce current funding levels.

To meet the budgetary target, agency appropriations would need to be reduced during the year or budgeted revertments would have to increase. Revertments are unspent appropriations that are returned to its source (in this case, the General Fund).

After reviewing OSPB's first report at its August meeting, the Committee asked OSPB to provide a list of projects initiated or referred to agencies for final cost-benefit analysis along with each project's contractor, relevant agencies, and projected savings.

The project is administered by a Governance Board appointed by the Governor. The attached report consists of spreadsheets detailing projects at the Arizona Health Care Cost Containment System (AHCCCS), the Department of Economic Security (DES), the Department of Health Services (DHS), and other agencies. We have attached the updated report provided at the Governance Board's October 27 meeting in lieu of providing the report submitted by OSPB, which was current only through the Board's September 28 meeting.

To date, it appears that there are 3 projects completed, all designed to increase federal Title XIX Medicaid reimbursement:

- Immunization Registry (AHCCCS/DHS): $135,000 annually
- ASH Inpatient Hospitalization (AHCCCS/DHS): unknown
- Juvenile Justice (Juvenile Corrections/AHCCCS): $250,000 annually

In another completed project, concerning the *Padilla vs. Rodgers* case, the courts have also ruled that the federal government must pay $3 million to the state for mandated court-ordered dialysis services provided to approximately 100 undocumented individuals. The Executive reports that AHCCCS has already drawn down approximately $3.5 million in federal funds representing state-only payments in FY 2003 and FY 2004. The $1.3 million of FY 2003 reimbursements will be reverted to the General Fund; the $2.2 million of FY 2004 reimbursements will be used to reduce a probable AHCCCS FY 2005 request. AHCCCS also anticipates that it will draw down $2.5 million in FY 2005 to help cover the costs of providing services for this population.

In addition to these projects, the summary lists 6 ongoing and 4 potential AHCCCS projects, 1 ongoing DHS project, 2 ongoing and 3 potential DES projects, and 2 other ongoing projects.

At its October 27 meeting, the Governance Board received updates from participating state agencies, but did not direct agencies to proceed with any new task orders.

The JLBC Staff would also note that many of the projects have notes indicating that savings would be used to offset supplemental appropriations or "reinvested in the Child Welfare System." Most of the actual or potential savings are in agencies with potential supplementals due to higher than expected caseloads. There are other projects, such as some in DES, where savings would represent reinvestments in programs -- these statements appear contrary to the intent of the FY 2005 budget that these revenue maximization initiatives generate $25 million in savings in the overall "balance sheet." The Executive reports, however, that any FY 2005 savings in DES would be used to reduce shortfalls within its child welfare budget.

RS/SSH:jb
Attachment

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DATE: November 5, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Kim Hohman, Senior Fiscal Analyst

SUBJECT: Attorney General - Department of Law - Report on New Staffing of Child Protective Services Attorneys

Request

The FY 2005 General Appropriation Act appropriated $4 million from the General Fund to the Division of Children, Youth and Families (DCYF) within the Department of Economic Security to fund 65 additional Attorney General legal staff positions working in DCYF. These positions are funded through the DCYF budget, but are still considered employees of the Office of the Attorney General (AG). The Chairman has requested that the Attorney General report on a quarterly basis, beginning October 15, 2004, on the status of hiring the new AG staff.

Recommendation

This report is for information only and no Committee action is required. The JLBC Staff does recommend, however, that the Committee request that future reports include information on the status of hiring new Attorney General positions funded from Federal Funds. The JLBC Staff estimates that the FY 2005 General Fund increase will result in an additional 28 AG legal staff.

The highlights of the report are:

- Of the 65 AG positions appropriated in the General Appropriation Act, 24 have been filled.
- At the end of the 1st Quarter of FY 2005, there were 10,434 children awaiting placement, up from 9,771 children a year ago. Of the 10,434, 2,935 children had been awaiting placement for longer than 24 months (compared to 2,618 a year ago).
- Since the 2nd Special Session in the fall of 2003, there have been a total of 119 jury trial requests and 16 actual jury trials. Of the amounts, 39 requests and 4 trials occurred in the 1st Quarter of FY 2005.

Analysis

The FY 2005 General Appropriation Act increased the DCYF budget by $4 million from the General Fund to provide 65 additional AG legal staff positions within the division. The increased appropriation provided funding for approximately 30 additional attorneys, 15 legal assistants, 15 legal secretaries, and 5 clerk typists. In addition, the General Fund appropriation is expected to draw down additional federal monies, which will fund approximately 28 attorney and support staff positions.

The increase in AG legal services funding within DCYF was in part due to changes made in the 2nd Special Session in the fall of 2003. Laws 2003, 2nd Special Session, Chapter 6 allowed individuals involved in parental rights termination cases to request jury trials. This type of legal proceeding requires more attorney hours, and therefore additional Attorney General resources. The additional funding appropriated in FY 2005 was provided to the AG to address an increase in the number of jury trial requests, as well as an increase in the number of dependency cases handled by the AG's Office. During the 2004 legislative session, the AG's Office indicated that there was a critical need to fill the additional staff positions. As a result, the Chairman has requested that the Attorney General report on the status of hiring new AG staff and the processing of dependency cases. Specifically, the Chairman requested that the reports include the following information: 1) the net number of Attorney General Child Protective Services positions filled at the end of each quarter; 2) the number of children (and cases) awaiting placement at the end of each quarter; and 3) the number of jury trials handled by the AG at the end of each quarter.

The AG has made some progress hiring new staff. As of October 1, the AG has on net filled 24 of the 65 positions appropriated in the FY 2005 General Appropriation Act. Of the 24 positions, 12 are attorneys, 2 are legal assistants, 3 are legal secretaries, and 7 are clerk typists.

The AG has also reported on the total number of children awaiting placement (children in the foster care system) and has displayed data for each month of the 1st Quarter of FY 2005. As of September 30, there were 10,434 children (5,870 cases) awaiting placement. Of this amount, 2,935 children (or 28%) had been awaiting placement for longer than 24 months. As a point of comparison, on June 30, 2004 there were 9,771 children awaiting placement, with 2,618 (or 27%) of these children waiting longer than 24 months for placement.

The AG reports a total of 39 jury trial requests during the 1st Quarter of FY 2005, or an average of 13 requests per month. In the 3rd and 4th Quarters of FY 2004 the number of jury trial requests also averaged 13 per month, for a total of 80 jury trial requests for that 6-month period. Of the 39 jury trial requests in the 1st Quarter of FY 2005, 4 resulted in trials actually being held. The information provided by the AG on jury trials is summarized in the following table:

Jury Trials
Parental Termination Cases

	Jury Trial Requests	Jury Trials Held	Jury Trials Held (as % of Requests)
FY 2004 (3rd & 4th Quarters)			
Jan. 2004 – June 2004	80	12	15%
FY 2005 (1st Quarter)			
July 2004 – Sept. 2004	39	4	10%
Total	**119**	**16**	**13%**

The Attorney General will continue to submit these reports through FY 2005.

RS/KH:ck

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DATE: December 9, 2004

TO: Senator Bob Burns, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director

FROM: Eric Jorgensen, Fiscal Analyst

SUBJECT: Arizona State Retirement System – Report on Contribution Rates

Request

The JLBC Subcommittee on Retirement Rates met October 21, 2004 to discuss the projected increase in the Arizona State Retirement System (ASRS) contribution rate.

Recommendation

This item is for information only and no Committee action is required. ASRS projects an increase in the contribution rate from 5.2% to 7.75% beginning in FY 2006. This increase produces an estimated FY 2006 cost of $22 million to state General Fund agencies and $51 million each to public school districts and teachers.

Analysis

The JLBC Subcommittee on Retirement Rates met on October 21, 2004 to discuss the projected increase in the ASRS contribution rate. ASRS projects an increase from 5.2% to 7.75%. Attachment 1 is the JLBC Staff presentation for the subcommittee and Attachment 2 and 3 are ASRS documents.

ASRS reported that investment losses in FY 2002 and FY 2003, as well as changes in the actuarial assumptions that determine the rate caused the majority of the rate increase. According to ASRS, nearly two-thirds of the increase (162 of the 255 basis points) is a result of losses in FY 2002 and FY 2003. However, this figure may be revised as previous ASRS estimates appear to included factors other than investment returns. The replacement of outdated actuarial tables accounts for a 65 basis point increase. The outdated tables were projected from a 1984 mortality table and did not accurately forecast the baby boomer mortality rates.

The delay in implementing the contribution rate has also driven up the projected rate. There are 2 reasons for the delay. First, the rate is calculated annually, but only implemented biennially. Therefore, in the second year of a biennium the retirement rate is not set at the level required to cover the costs of the system. Second, the rate is calculated each November based on data ending the previous June. This rate is not implemented until the following July, making the data a year old when the rate is implemented. Thus, in the first year of the biennium, the rate is already 1 year old, and in the second year, it is 2 years old.

(Continued)

The following chart shows the ASRS breakdown of the increase:

ASRS Contribution Rate Factors FY 2004 to FY 2006	
Old Rate (Implemented FY 2004)	5.20%
Investment Losses and Gains	1.54%
New Mortality Tables (Actuarial Assumptions)	0.65%
Delay in adopting new contribution rates	0.48%
Extension of rural health insurance subsidy	0.03%
Change in the Funding Period	-0.06%
Adjustment to PBI Reserve	-0.02%
Change in the Service Purchase Cost	-0.17%
Decrease in interest accrual rate for member accounts (from 8% to 4%)	-0.15%
Total Increase	2.50%
New Rate	**7.50%**

ASRS is currently funded at 87.5% of liabilities. By raising the rate, the retirement system will be able to cover the normal cost of providing benefits and begin to decrease its unfunded liability. However, ASRS projects that future rate increases will be necessary since gains and losses are recognized over a 10-year period. Hence, a component of the losses in FY 2002 will be part of the rate until FY 2012. This helps to smooth out the fluctuations in the contribution rate. Based on current assumptions, ASRS expects the rate to rise above 10% within 6 years.

At the JLBC Subcommittee meeting, options were discussed to reduce the effects of the rate increase and prevent similar situations in the future. The increase results in a take-home pay decrease of $25.50 for every $1,000 of pre-tax pay for state employees, teachers and other participants in ASRS. Two options were presented to limit the impact on the employees. The first option was a salary increase. This would cost state General Fund agencies about $26 million to offset the contribution as well as other Employee Related Expenses. Instead of providing a salary increase, the employer could contribute more then the current 50% to cover the employee’s portion of the increase. Employers in the Public Safety Personnel Retirement System (PSPRS) use this method to reduce employee costs. This alternative would cost General Fund agencies an additional $22 million. The cost of either alternative is in addition to a $22 million increase in employer contributions. The total cost of the increase if the burden is shifted from the employee to the employer is between $44 million and $48 million to General Fund agencies. In a memo announcing the projected rate increase the Arizona Department of Administration indicated that the Governor will seek funding to maintain employee take home pay.

Options for preventing similar situations included raising the floor on contribution levels. Currently, contribution levels cannot fall below 2%. In times of high investment returns, setting the contribution rate higher than is needed creates a surplus that could offset future losses. This assumes no benefit increases. There was also discussion of changing some of the assumptions, including the 8% rate of return on investments. Currently, the actuary performs an experience study every 5 years to assure that assumptions are realistic.

The Chairman submitted additional questions to ASRS after the November meeting. ASRS’s response to those questions is found in Attachment 3.

RS/EJ:jb